

UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF INDIANA  
HAMMOND DIVISION

IN RE:	)	
	)	
HERBERT RONALD KARNER and	)	CASE NO. 05-61512 jpk
ANNA RUTH DAVIS KARNER,	)	Chapter 7
	)	
Debtors.	)	
*****	)	
FRED DAVIS,	)	
	)	
Plaintiff,	)	
v.	)	ADVERSARY NO. 05-6108
	)	
ANNA RUTH DAVIS KARNER,	)	
	)	
Defendant.	)	

DECISION ON THE APPLICATION OF COLLATERAL ESTOPPEL

This adversary proceeding is before the Court on the Plaintiff, Fred Davis' ("Davis"), First Amended Complaint to Determine Dischargeability of Debt filed against the debtor Anna Ruth Davis Karner ("Karner"). In the complaint, Davis asserts that certain of Karner's debts to him should be excepted from discharge pursuant to 11 U.S.C. § 523(a), particularly §523(a)(4). Davis also contends the issues of exception from discharge addressed by the complaint in this adversary proceeding are subject to principles of collateral estoppel, arising from a judgment entered in state court.

This Court has jurisdiction over this adversary proceeding pursuant to 28 U.S.C. § 1334(b), 28 U.S.C. § 157(a), and N.D.Ind.L.R. 200.1(a)(2). This matter constitutes a "core" proceeding as defined by 28 U.S.C. § 157(b)(2)(I).

**I. Statement of the Record**

The adversary proceeding was initiated by a complaint filed on July 5, 2005. An answer to the complaint was filed by Karner, proceeding *pro se*, on July 27, 2005: Karner filed a handwritten letter on July 27, 2005, which this Court deemed to be an answer. A preliminary pre-trial conference was held on October 5, 2005, which resulted in an order entered on October 13,

2005. This order required Davis to file an amended complaint and provided that Karner's answer to the original complaint would be deemed to be her answer to the amended complaint, without her having to file a separate answer, unless she desired to file a separate answer. This order also required counsel for Davis to file of record exemplified copies of all pleadings filed in the prior state court action between the parties, including the complaint, motions to dismiss, answer, any amendments to the pleadings, and all documents filed by either party with respect to the plaintiff's motion for judgment filed in that proceeding, and to provide a copy of those documents to Karner. Davis' first amended complaint was filed on November 7, 2005, and Karner filed a separate answer to the amended complaint on December 1, 2005. Davis' counsel filed the state court record on December 22, 2005, and provided a copy of that record to Karner.

Pursuant to the Court's order entered on January 27, 2006, a conference was held with the parties on February 22, 2006, to determine the course of further proceedings in the case. The result of that conference was the Court's order entered on February 28, 2006. That order provided that issues of collateral estoppel arising from the state court proceedings would be determined on the basis of the record of those proceedings filed with the Court on December 5, 2005. Because those issues are purely questions of law with which the Court is thoroughly familiar, the Court determined that the submission of briefs by the parties would not aid its determination. The February 28, 2006, order stated:

As asserted in the complaint, prior to the defendant's initiation of her Chapter 7 bankruptcy case, the plaintiff obtained a judgment in case number 45D05-0110-CP-484 in the Superior Court of Lake County, Indiana. This judgment was entered following summary judgment proceedings in that court, and made certain determinations with respect to the obligations found to be due by the defendant to the plaintiff. The preliminary issue to be resolved in this adversary proceeding is the extent to which the judgment of the Lake Superior Court is entitled to collateral estoppel effect with respect to the plaintiff's assertions under 11U.S.C. § 523(a)(4) in this adversary proceeding. The Court determines

that this issue can be determined from the record presently before the Court . . .

See, Docket Entry #27

This case is therefore before the Court on a designated record to determine the issues of collateral estoppel which may arise from the judgment of the Lake County, Indiana, Superior Court entered on May 5, 2005 in the case of Fred Davis v. Anna Davis Karner, Cause Number 45D05-0110-CP-484, by which Davis was granted final judgment against Karner through the mechanism of a summary judgment. Technically, this method of determination is akin to a summary judgment sought by the plaintiff to determine all issues between all parties in the adversary proceeding. However, it is unlike a summary judgment in that there are no contested genuine issues of material fact: the state court record – the only material outside the pleadings necessary for the Court's determination – is before the Court, and there are no issues of fact as to that record. The Court deems this procedure to be outside the true scope of Fed.R.Bank.P. 7056/Fed.R.Civ.P. 56, and the Court deems the submission of materials in accordance with the procedures implemented by those rules to be both superfluous and an unnecessary expenditure of time and expense by the litigants. The issue of the collateral effect to be given to the judgment of the Lake County, Indiana, Superior Court entered on May 5, 2005 in the case of Fred Davis v. Anna Davis Karner, Cause Number 45D05-0110-CP-484 is simply before the Court for determination as a question of law based upon the only material record necessary for that review and decision.<sup>1</sup>

## **II. Statement of Facts Pertinent to Decision**

Karner filed a petition for relief under Chapter 7 of the United States Bankruptcy Code on March 31, 2005, thereby initiating Case Number 05-61512. Davis is designated as a

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<sup>1</sup> Because the policies of *Timms v. Frank*, 953 F.2d 281, 285 (7th Cir. 1992) are not implicated by this procedure, the Court has not provided Karner, as a *pro se* litigant, with the notice of procedures, and of the consequences of failure to submit opposing materials of record, imposed by that decision.

creditor in that case.

On October 19, 2001, Davis had sued Karner in the Lake County Superior Court, in Case Number 45D05-0110-CP-484. The complaint principally alleged that Karner had converted approximately \$19,900.00 of the Davis' funds, in contravention of I.C. 34-24-3-1. It was alleged that Davis gave Karner limited authority regarding funds at Bank One, under Account No. 000185 050 243 111, and that Karner's authority was limited to paying for Davis' burial and/or the directing of funds at his request. The complaint further alleged that, several months after the granting of said authority, Davis discovered that Karner had withdrawn \$19,900.00 in funds from the account for her own use. Karner, who was represented by counsel, filed an answer which denied all of the material averments of the complaint and which included a flurry of largely irrelevant affirmative defenses. Karner, by counsel, also filed a counterclaim which in multiple counts branded the complaint as frivolous, an act of malicious prosecution, an abuse of process, and an intentional infliction of emotional distress – essentially an abomination to the natural order of things.

Subsequently, Davis filed a motion for summary judgment, which the state court granted, and a judgment in the amount of \$83,329.17 was entered against the debtor. The judgment included actual damages in the amount of \$18,900.00,<sup>2</sup> pre-judgment interest in the amount of \$6,229.17, treble damages in the amount of \$56,700.00 and attorneys' fees in the amount of \$1,500.00.

Pursuant to this Court's order of October 13, 2005 Davis filed an amended complaint on November 7, 2005 and attached copies of the record of the state court proceeding which included: the Complaint filed by Davis, the Answer and Counter Claim filed by Karner along with Davis' answer thereto, and the Motion for Summary Judgment which included Requests for

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<sup>2</sup> Apparently, the Defendant received a \$1,000.00 credit for amounts paid prior to the commencement of the state court litigation.

Admissions, an Order deeming the Requests admitted, bank withdrawal receipts and an affidavit of the Plaintiff. As required by the Court's October 13, 2006, order, the plaintiff was directed to file of record, and provide to the defendant, exemplified copies of, "all pleadings including the complaint, motion to dismiss, the answer and any amendments to the foregoing, all documents filed either by the plaintiff or defendant with respect to the plaintiff's motion for summary judgment." See Docket Entry #16. This was done on December 5, 2005 and consisted of the items listed above which were originally attached to the plaintiff's Complaint, along with a copy of the judgment entered by the Honorable Robert Pete on May 5, 2005.

The following materials constitute the designated record: Davis' state court Complaint and all attachments thereto, the Answer and Counterclaim filed by Karner and all attachments thereto, Davis' answer to the counterclaim and all attachments thereto, the Motion for Summary Judgment (which included as exhibits Requests for Admissions, an Order deeming the Requests admitted, bank withdrawal receipts and an affidavit of the Plaintiff), and the state court Judgment entered against the defendant.

Because Karner's answer in the state court proceeding denied every averment of Davis' complaint, no facts were derived from the pleadings in the Lake Superior Court's determination of Davis' summary judgment motion. The factual record before that court was exclusively comprised of Davis' submissions – Karner filed nothing in response to Davis' motion. The Request for Admissions – deemed admitted by the state court – establish that Karner made 11 separate withdrawals – each on a designated date and in a designated amount – from Davis' account; the withdrawal receipts document these withdrawals. There is nothing in the admissions apart from the facts that designated amounts were withdrawn on designated dates from the account. The only other factual material before the Lake Superior Court with respect to Davis' motion for summary judgment was Davis' affidavit, the entirety of which – omitting

caption, signature and jurat, is the following:

Plaintiff/Affiant, FRED DAVIS, does affirm and assert as follows:

1. He opened a bank account in his name and in the name of Anna Davis Karner on or about 1999.
2. This bank account was not a typical "joint account," in that Anna Karner had no interest or rights in the monies in the account.
3. The sole purpose of this bank account was to (a) pay for his burial cost should the need arise and/or (b) be "insurance" for any unexpected occurrences which may need emergency funds (ie. his car breaking down ...).
4. Anna Karner did at all times know that this was the purpose of said bank account.
5. Anna Karner had no authority beyond that which is described in #3 to withdraw funds or otherwise have access to the bank account.
6. Between January of 2000 and August of 2000 Anna Karner did receive approximately \$18,900.00 to which she has yet to pay back.
7. The withdrawal of these funds were without the knowledge or consent or authority of Fred Davis.
8. He took reasonable measures short of litigation to allow Anna Karner to repay the withdrawals.
9. Further Affiant saith not.

The judgment entered by the Lake Superior Court is in its entirety as follows:

#### ORDER

This matter before the Court the 31<sup>st</sup> day of August, 2004 for scheduled hearing on Motion for Summary Judgment filed by plaintiff, Fred Davis, who appears with counsel, James E. Foster, Defendant, Anna Davis Karner, does not appear in person or by counsel for this hearing. The Court hears argument and being duly advised FINDS there are no genuine issues of material fact concerning Fred Davis' entitlement of damages as prayed. The Court further finds the attorney fee request is reasonable and shall be granted. The Court lastly finds there is no just reason for delay and final judgment should be entered in favor of Davis and directs preparation of this Order which provides, in some particulars, as follows:

1. The court finds that Anna Davis Karner removed from account # 000185 050 243 111 twelve separate withdrawals as more particularly described in Request for Admissions 1 thru 11 in a total sum of \$19,900.00 from January 3, 2000, through August 8, 2000, and repaid the sum of \$1,000.00 on April 26, 2000.
2. The Court further finds the money withdrawn was the sole property of Fred Davis and the withdrawals by Anna

Davis Karner were without the knowledge, consent or authority of Fred Davis and contrary to the specific grant of authorization, to Anna Davis Karner, which was to make withdrawals only for the benefit of Fred Davis.

3. That the Court further finds the loss to Fred Davis includes \$18,900.00 plus pre-judgment interest from the dates of the individual withdrawals as reflected in Request for Admissions 1 thru 11 as specified

- \$1,400.00 withdrawn 01/30/00
- \$1,000.00 withdrawn 04/10/00
- \$1,000.00 withdrawn 04/17/00
- \$1,000.00 repaid 04/26/00
- \$1,000.00 withdrawn 06/05/00
- \$1,500.00 withdrawn 06/29/00
- \$1,500.00 withdrawn 07/12/00
- \$1,500.00 withdrawn 07/17/00
- \$1,500.00 withdrawn 07/21/00
- \$1,500.00 withdrawn 07/25/00
- \$1,500.00 withdrawn 08/07/00
- \$3,000.00 withdrawn 08/08/00

As shown by Exhibit A attached to this order the ipre [sic] judgment interest as of 8-31-04 was \$6,229.17.

4. The Court further finds that the actions, of Anna Davis Karner, in withdrawing the funds of Fred Davis, constitute conversion entitling Fred Davis to an amount not to exceed 3 times the actual damages plus attorney fees pursuant to I.C. 34-24-3-1. The court finds that the "punitive" or "treble" damages in this case should be three thime [sic] the actual damages of \$18,900.00 or \$56,700.00.

5. That further Fred Davis is entitled to attorney fees pursuant to I.C. 34-24-3-1 and a reasonable and modest attorney fee in this matter is the sum of \$1,500.00.

6. The Court there finds that Fred Davis is entitled to a total judgment of \$83,329.17 which includes actual damages of \$18,900.00 plus pre judgment interest of \$6,229.17, plus treble damages of \$56,700.00 plus attorney fees of \$1,500.00 as of August 31, 2004.

IT IS THEREFORE, ORDERED, ADJUDGED AND DECREED that summary judgment is granted in favor of plaintiff, Fred Davis, and against defendant, Anna Davis Karner, and Judgment is entered in favor of Fred Davis and against Anna Davis in the sum of \$83,329.17 which includes actual damages plus pre judgment interest and treble damages plus 1,500.00 for attorney fees plus the costs of this action.

Statutory interest to run on this judgment from the date of the finding to wit August 31, 2004.

IT IS FURTHER ORDERED there is no just reason for delay and this ruling is entered as a final judgment pursuant to Indiana Trial Rule 56(C).

SO ORDERED.

**III. Analysis**

11 U.S.C. § 523(a)(4) provides that a debt is excepted from discharge if the debt is "for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny." In an adversary proceeding to determine the nondischargeability of a debt, the burden of proof is on the plaintiff as to each element of the statutory exception to discharge; *In re Kreps*, 700 F.2d 372, 376 (7<sup>th</sup> Cir. 1983); *Zygulski v. Daugherty*, 236 B.R. 646, 653 (Bankr. N.D.Ind. 1999), citing, *Matter of Scarlata*, 979 F.2d 521, 524 (7<sup>th</sup> Cir. 1992). Furthermore, exceptions to discharge are to be construed strictly against the creditor and liberally in favor of the debtor; *Matter of Scarlata*, 979 F.2d at 524 (citing, *In re Zarzynski*, 771 F.2d 304, 306 (7<sup>th</sup> Cir. 1985)). The United States Supreme Court has held that the standard of proof in nondischargeability proceedings under § 523(a) is a preponderance-of-evidence standard rather than the more stringent standard of clear and convincing evidence; *Grogan v. Garner*, 498 U.S. 279 (1991).

Davis asserts that the facts already determined by the state court's decision on his motion for summary judgment give rise to collateral estoppel with respect to his complaint in this adversary proceeding. It is undisputed that collateral estoppel applies in the bankruptcy context; *In re Jones*, 180 B.R. 531, 532 (Bankr. S.D.Ind. 1994) citing *Grogan V. Garner*, 498 U.S. 279. n. 11, 111 S.Ct. 654, 658, n.11, 112 L.E.2d 755 (1991). A state court judgment is entitled to full faith and credit in bankruptcy proceedings; 28 U.S.C. § 1738 (West 2006); *Matter of Bulic*, 997 F.2d 299, 304 (7<sup>th</sup> Cir. 1993). The effect of a judgment in subsequent litigation is determined by the law of the jurisdiction that rendered the judgment. *In re Catt*, 368 F.3d 789, 790-91 (7<sup>th</sup> Cir. 2004); *Wolverine Mutual Insurance v. Vance*, 325 F.3d 939 (7<sup>th</sup> Cir. 2003); *In re Scarborough*, 171 F.3d 638 (8<sup>th</sup> Cir. 1999) *cert. denied* 528 U.S. 931 (1999); *In re Keaty*, 397 F.3d 264, 270 (5<sup>th</sup> Cir. 2005) (discussing the requirement of "actually litigated"); *Brokaw v. Weaver*, 305 F.3d 660, 669 (7<sup>th</sup> Cir.2002) ["The preclusive effect of a state court



judgment in a federal case is a matter of state rather than of federal law"]. Thus, the effect of the Lake Superior Court's Judgment for collateral estoppel purposes is governed by Indiana law.

Collateral estoppel bars the resuscitation of issues that have been previously litigated. Under Indiana law, the elements for the application of collateral estoppel are the following: (1) the issue sought to be precluded is the same as that involved in a prior action, (2) the issue was actually litigated, (3) determination of the issue was essential to the final judgment, and (4) the party to be estopped was fully represented in the prior action; *In re Jones*, 180 B.R. 531, 533 n.3 (Bankr. S.D.Ind. 1994); see also *Millenium Club, Inc. v. Avila*, 809 N.E.2d 906 (Ind.Ct.App. 2004) citing *Pritchett v. Heil*, 756 N.E.2d 561 (Ind.Ct.App. 2001); *Infectious Disease of Indianapolis, P.S.C. v. Toney*, 813 N.E.2d 1223, (Ind.Ct.App. 2004); *Tofany v. NBS Imaging Systems, Inc.*, 616 N.E.2d 1034 (Ind. 1993).<sup>3</sup> As stated in *Segovia v. State of Indiana*, 666 N.E.2d 105, 107 (Ind. App. 1996):

In order to apply the doctrine of collateral estoppel, the court must engage in a two step analysis: "(1) determine what the first judgment decided; and (2) examine how that determination bears on the second case." *Webb v. State*, 453 N.E.2d 180, 183 (Ind. 1983), *reh. denied, cert. denied*, 465 U.S. 1081, 79 L. Ed. 2d 767, 104 S. Ct. 1449 (1984) (citing *United States v. Mespouledé*, 597 F.2d 329 (2d Cir. 1979)).

In addition, in the situation where a different claim is asserted in a subsequent lawsuit, collateral estoppel will still apply if an issue of fact material to both actions was determined in the prior case.<sup>4</sup> As stated in *In re Staggs*, 178 B.R. 767, 773 (Bankr. N.D. Ind. 1994) [citing the

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<sup>3</sup> Collateral estoppel applies under federal law under the same criteria; *Levinson v. United States*, 969 F.2d 260, 264 (7<sup>th</sup> Cir.1992) (citing *Klingman v. Levinson*, 831 F.2d 1292, 1295 (7<sup>th</sup> Cir.1987); *In re Massey*, 228 B.R. 686, 690 (Bankr. S.D.Ind. 1998); *In re Busick*, 264 B.R. 518, 522 (Bankr. N.D.Ind. 2001); *In re Staggs*, 177 B.R. 92, 95 (N.D.Ind. 1995); *In re Lehman's Inc. of Andersen*, 163 B.R. 814, 816 (S.D.Ind. 1994).

<sup>4</sup> This is certainly relevant in the matter before the Court now – in the state court action the plaintiff brought an action based on the tort of conversion, and now brings a different claim

Restatement (Second) of Judgments]:

When an issue of fact or law is actually litigated and determined by a valid and final judgment, and the determination is essential to the judgment, the determination is conclusive in a subsequent action between the parties, whether on the same or a different claim . . . A review of Indiana case law shows that this general rule is followed by the Indiana courts as well. *Bulic*, 997 F.2d at 304 n. 6 (quoting *Bicknell*, 118 Bankr. at 664 (citing *Hardesty v. Bolerjack*, 441 N.E.2d 243, 245 (Ind. App. 1982))).

In determining whether or not collateral estoppel applies in a subsequent proceeding, the court must examine the entire record before the court which entered the prior decision. As stated in *Segovia*, *supra.*, 666 N.E.2d at 107:

[Determining] what the first judgment decided involves an examination of the record of the prior proceedings including the pleadings, evidence, charge and any other relevant matters. 453 N.E.2d at 184. The court must then decide whether a reasonable jury could have based its verdict upon any factor other than the factor of which the defendant seeks to foreclose consideration. *Id.* If the jury could have based its decision on another factor, then collateral estoppel does not bar relitigation. *Id.*

As the state court has already entered a judgment, and made certain findings against the defendant for conversion under Indiana law – this Court must now determine whether or not the issues decided rise to the level required for the debt to be excepted from discharge pursuant to 11 U.S.C. § 523(a)(4).

In his Amended Complaint, Davis alleges that the foregoing debt, including the award of attorneys' fees, is excepted from discharge under § 523(a)(4) for, specifically, embezzlement or larceny. For the purpose of determining dischargeability, embezzlement and larceny are defined by federal common law. *Valentine v. Valentine*, 104 B.R. 67, 70 (Bankr. S.D.Ind. 1988). Embezzlement, under § 523(a)(4), is defined as the fraudulent appropriation of the creditor's property by the debtor to whom it has been entrusted or into whose hands it has

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before the bankruptcy court for dischargeability and seeks the imposition of collateral estoppel for certain issues previously litigated.

lawfully come. *Dobek v. Dobek*, 278 B.R. 496, 509 (Bankr. N.D.Ill. 2002) (citing, *Pierce v. Pyritz*, 200 B.R. 203, 205 (Bankr. N.D.Ill. 1996); *see also*, *Matter of Weber*, 892 F.2d 534, 538 (7<sup>th</sup> Cir. 1989)). On the other hand, larceny is where the original taking of the property was not lawful. *Id.* at 509-10. Embezzlement differs from larceny only in that the original taking was lawful. *In re Rose*, 934 F.2d 901, 903 (7<sup>th</sup> Cir. 1991). As a result, by definition, before a creditor can make a claim of nondischargeability for embezzlement or larceny, it must show that the property allegedly embezzled/larcened by the debtor was property of the creditor. *Dobek*, 278 B.R. at 509-10. There is no question here that the funds alleged to have been misappropriated were Davis' property.

Whether or not the appropriate context for Davis' § 523(a)(4) action is "larceny" or is "embezzlement" is a fine line. On the one hand, it could be asserted that this property originally came into the hands of the debtor lawfully; that is, the creditor consented to the debtor's being a signatory on the account; the action then sounds in "embezzlement". On the other hand, given the allegation that the debtor was not authorized to make withdrawals of the nature of those she made from the account, it could be contended that she came into possession of the funds unlawfully, which would cause this to be a case of possible larceny. Because the "property" for the purposes of Davis' § 523(a)(4) action is the funds withdrawn from the account, rather than the account itself, the allegations probably fit the case more under the "larceny" prong. As we will see, the strict categorization doesn't matter – the essential elements of the federal nondischargeability action are the same for both.

The elements of "embezzlement" under 11 U.S.C. § 523(a)(4) have been well-defined by the United States Court of Appeals in *In re Weber*, 892 F.2d 534, 538-9 (7<sup>th</sup> Cir. 1989) as follows:

Section 523(a)(4) of the bankruptcy code does not allow a debtor to discharge a debt incurred as a result of the debtor's embezzlement. Bankruptcy courts define embezzlement as the

"fraudulent appropriation of property by a person to whom such property has been entrusted or into whose hands it has lawfully come." *Moore v. United States*, 160 U.S. 268, 269, 16 S.Ct. 294, 295, 40 L.Ed. 422 (1895), *quoted in In re Bevilacqua*, 53 B.R. 331, 333 (Bankr.S.D.N.Y.1985), *In re Myers*, 52 B.R. 901, 905 (Bankr.E.D.Va.1985), *In re Graziano*, 35 B.R. 589, 594 (Bankr.E.D.N.Y.1983); *see also In re Belfry*, 862 F.2d 661, 662 (8<sup>th</sup> Cir.1988). To prove embezzlement, the creditor must show by clear and convincing evidence that (1) the debtor appropriated funds for his or her own benefit; and (2) the debtor did so with fraudulent intent or deceit. *In re Taylor*, 58 B.R. 849, 855 (Bankr.E.D.Va.1986); *In re James*, 42 B.R. 265, 267 (Bankr.W.D.Ky.1984); *In re Storms*, 28 B.R. 761, 765 (Bankr.E.D.N.C.1983); *Graziano*, 35 B.R. at 595.

Ablan initially argues that the bankruptcy court should have applied the embezzlement and conversion laws of Wisconsin. Although he cites no authority for this proposition, and admits that ultimately the issue of nondischargeability is a question of federal law, he claims that state law is "useful" in defining the elements of embezzlement. Ablan claims that the Wisconsin cases he cites "do not in any event conflict with the [federal standards]"; his analysis of this caselaw, however, leads him to conclude that "[t]he act of depositing [another's] funds into one's account, thereafter causing them ... to be dispersed for one's own purposes or uses is the kind of evidence which *would compel the conclusion that embezzlement has occurred.*" (emphasis added). Under federal law, such a conclusion is not compelled since the creditor must also prove that the dispersal occurred with fraudulent intent. Thus, Ablan had to prove more than just the fact that Weber used the sales proceeds to pay off his personal debts; he had to prove that Weber did so with fraudulent intent.

The element of fraudulent intent is a constant in federal decisions under § 523(a)(4)'s "embezzlement" and "larceny" prongs; See, e.g., *In re Dempster*, 182 B.R. 790, 802 (Bankr. N.D. Ill. 1995); *In re Fields*, 2005 WL 2205787 (Bankr. C.D. Ill. 2005); *In re Brady*, 101 F.3d 1165, 1172-3 (6<sup>th</sup> Cir. 1996); *In re Rogstad*, 126 F.3d 1224, 1228 (9<sup>th</sup> Cir. 1997); *In re Fuget*, 339 B.R. 702, 707 (Bankr. S.D. Iowa 2006); *In re Lammers*, 2005 WL 1498336 (Bankr. M.D. Fla. 2005).

In order to sustain an action for "embezzlement" or "larceny" under 11 U.S.C. § 523(a)(4), the plaintiff must establish not only that the debtor exercised unauthorized

control over property, but that the debtor had a fraudulent intent in doing so.

Under this framework, the Lake Superior Court, in its judgment, found as follows:

1. The Court finds that Anna Davis Karner removed from account # 000185 050 243 111 twelve separate withdrawals as more particularly described in Request for Admissions 1 thru 11 in a total sum of \$19,900.00 from January 3, 2000, through August 8, 2000, and repaid the sum of \$1,000.00 on April 26, 2000.

2. The Court further finds the money withdrawn was the sole property of Fred Davis and the withdrawals by Anna Davis Karner were without the knowledge, consent or authority of Fred Davis and contrary to the specific grant of authorization, to Anna Davis Karner, which was to make withdrawals only for the benefit of Fred Davis.

4. The Court further finds that the action, of Anna Davis Karner, in withdrawing the funds of Fred Davis, constitute conversion entitling Fred Davis to an amount not to exceed 3 times the actual damages plus attorneys fees pursuant to I.C. 34-24-3-1. The Court finds that the "punitive" or "treble" damages in this case should be three times [sic] the actual damages of \$18,900.00 or \$56,700.00.

See, State Court Order (¶s 1, 2 & 4)

The place to start is to analyze the elements for conversion, the tort for which the Defendant was found liable, under state law. Indiana Code 35-43-4-3 provides in pertinent part:

a) A person who knowingly or intentionally exerts unauthorized control over property of another person commits criminal conversion, a Class A misdemeanor.

See, Indiana Code 35-43-4-3(a) (West 2006).

Indiana Code 35-43-4-1 defines the "exertion of control over property" and "unauthorized" as follows:

(a) As used in this chapter, "exert control over property" means to obtain, take, carry, drive, lead away, conceal, abandon, sell, convey, encumber, or possess property, or to secure, transfer, or extend a right to property.

(b) Under this chapter, a person's control over property of another person is "unauthorized" if it is exerted:

(1) Without the other person's consent;

The critical element of the tort of conversion under Indiana law is the exercise of unauthorized control over the property of another: "To constitute the tort of conversion, there must be an appropriation of the property of another;" *Stevens v. Butler*, Ind. App., 639 N.E.2d 662, 666 (1994). As stated in *Indiana & Michigan Electric Company v. Terre Haute Industries, Inc.*, Ind. App., 507 N.E.2d 588, 610 (1987):

Conversion is a tort involving the appropriation of personal property of another to the tortfeasor's own use and benefit, to the exclusion of and in defiance of the owner's rights, under an inconsistent claim of title; mens rea is not an essential element. 6 I.L.E. *Conversion* sec. 11 (1958). Thus, the mere existence of the tort does not necessarily carry with it the imputations of malice, so even if the tortfeasor acted in good faith in assuming dominion over the property, such is no defense. *Howard Dodge & Sons, Inc. v. Finn* (1979), 181 Ind.App. 209, 391 N.E.2d 638. Lack of consent by the owner is an element. 6 I.L.E. *Conversion* sec. 13 (1958).

The state court judgment granted to Davis has no finding of anything remotely approaching a determination of fraudulent intent on the part of Karner. The record on which the judgment was based has no fact which implicates fraud – the record establishes only the facts necessary to provide the elements of conversion under Indiana law, i.e., the exercise of unauthorized control over property of another. Establishment of the federal action for an exception to discharge for "embezzlement" or for "larceny" requires establishing not only that property was misappropriated, but also establishing fraudulent intent, which entails the use to which the misappropriated property was placed and the intent of the misappropriator in doing the act of misappropriation. Based upon the record in the Lake Superior Court, the judgment granted to Davis fails to establish the critical federal element of Karner's fraudulent intent, and that judgment has no collateral estoppel effect in this adversary proceeding with respect to actions for "embezzlement" or for "larceny" under 11 U.S.C. § 523(a)(4) because the issue of fraudulent intent was never litigated in the state court proceeding.

11 U.S.C. § 523(a)(4) also excepts from discharge debts arising from a person's "fraud or defalcation while acting in a fiduciary capacity." There is no collateral estoppel effect in this context, either. First, authorization by one person to another to access the former's bank account for certain purposes does not a "fiduciary" make – Davis retained full control over the account, and the concept of "fiduciary" established by applicable caselaw requires far more than this case presents to establish the necessary elements for "fiduciary" capacity; *See, In re Marchiando*, 13 F.3d 1111 (7<sup>th</sup> Cir. 1994); *In re Frain*, 230 F.3d 1014 (7<sup>th</sup> Cir. 2000); *In re Tsikouris*, 340 B.R. 604 (Bankr. N.D. Ind. 2006). Additionally, the state court record fails to establish that any determination of fraud or of defalcation by Karner was made: the judgment is based on simple conversion, which merely required Davis to establish that Karner exercised unauthorized control over the funds in the account, without any consideration of her intent in doing so.<sup>5</sup>

The record in the case of Fred Davis v. Anna Davis Karner, Cause Number 45D05-0110-CP-484, including the judgment of the Lake County, Indiana, Superior Court entered on May 5, 2005, does not establish that facts/issues necessary to give collateral estoppel effect to that judgment with respect to the plaintiff's claims in this adversary proceeding, were determined in that state court case.

IT IS ORDERED that there is no collateral estoppel effect in this adversary proceeding arising from the judgment of the Lake County, Indiana, Superior Court entered on May 5, 2005, in the case of Fred Davis v. Anna Davis Karner, Cause Number 45D05-0110-CP-484.

IT IS FURTHER ORDERED that a pre-trial/scheduling conference will be held in open

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<sup>5</sup> Although not really before the Court, it should also be noted that the entire lack of any determined issue concerning Karner's intent in the state court record precludes any collateral estoppel effect under both 11 U.S.C. § 523(a)(2) [*See, In re Hostetter*, 320 B.R. 674 (Bankr. N.D.Ind. 2005)] and under 11 U.S.C. § 523(a)(6) [*See, In re Whitters*, 337 B.R. 326 (Bankr. N.D.Ind. 2006)].

court on **November 30, 2006, at 9:30 A.M.** to determine the course of further proceedings in this adversary proceeding. It will be necessary for the defendant Anna Ruth Davis Karner and counsel for the plaintiff to personally appear before the Court at that conference.

Dated at Hammond, Indiana on October 18, 2006.

/s/ J. Philip Klingeberger  
J. Philip Klingeberger, Judge  
United States Bankruptcy Court

Distribution:  
Attorney for Plaintiff  
Defendant